

**"FRONT LOADED" ACCRUAL RATE FOR SPECIAL SERVICES:  
IMPLICATIONS FOR PRE-1984 EMPLOYEES WHO "CROSS OVER"  
TO THE NEW RETIREMENT SYSTEM.**

Section 8415(d) of the draft bill (p.26, April 3 discussion draft) establishes a defined benefit accrual rate of 1.7% of final average salary for each of the first 20 years of service by a "special service" employee, with a 1% accrual rate for any additional service. The Foreign Service draft amendment would link computation of FS annuities to 8415(d).

Title III of the draft bill (p. 99 et seq.) provides for pre-1984 employees to elect coverage under the new system's rules. Sec. 302 (a)(1)(B) (p.104) states that pre-1984 service is creditable for the purposes of establishing annuity eligibility.

Employees who elect to "cross over" get an annuity computed under two different formulas. The annuity for pre-crossover experience is computed by Chapter 83, old system rules. The annuity for post-crossover experience is computed under Chapter 84 rules. (Sec. 302 (a) (4) and (5), p. 105-106).

Post-crossover service is thus added to pre-crossover service to see if the employee has the total service needed to retire. But, for purposes of annuity computation, no such add on is mandated.

Therefore, a special service employee who crosses over will receive up to 20 years of annuity benefit at the 1.7% rate, regardless of how much service he or she had before crossover.

Example: (1) Able joins the FS in 1967 and has 20 years of service in the FS when he crosses over in 1987. He retires in 2007 with 40 years service. His annuity is  $20 \times 2\%$  (for the pre-crossover service), plus  $20 \times 1.7\%$ , or 74% altogether for 40 years service. (If Able's pre-crossover service were counted for purposes of determining his annuity computation for new system service, his 20 years of new system service would be computed at 1%, and his total annuity would be 60% of his final average salary.)

(2) Baker joins the FS in 1977 and has 10 years of pre-crossover service. He retires in 2007 with 30 years of service. His annuity is  $10 \times 2\%$  plus  $20 \times 1.7\%$ , or 54% altogether. If the less generous rule were used, his annuity would be  $10 \times 2\%$ , plus  $10 \times 1.7\%$ , plus  $10 \times 1\%$ , for 47% altogether.)

(3) Charles joins the FS in 1982 and has 5 years of pre-crossover service. He retires in 2007 with 25 years of service. His annuity is  $5 \times 2\%$  plus  $20 \times 1.7\%$ , or 44% altogether. If the less generous rule were used, his annuity would be  $5 \times 2\%$ , plus  $15 \times 1.7\%$ , plus  $5 \times 1\%$ , for 40.5% altogether.

(4) Davis, Early, and Fox join the FS in 1987 and serve 40, 30, and 25 years respectively. Their annuities are 54%, 44%, and 39% respectively.

#### Observations:

As written, the discussion draft is inconsistent in its philosophy with respect to special service annuity computation. The general philosophy, as set down in 8415(d) gives special service employees larger annuities on the assumption that careers will be shorter than normal. Service beyond 20 years thus gets no special bonus, since such service indicates that the employee is approaching more normal career length.

However, for special service employees with the option to crossover, the discussion draft makes no such distinction about shorter or longer careers. Special service employees can get a full 20 years of credit at the higher accrual rate, regardless of how much pre-crossover service they have. Thus Able, in our example above, works 40 years without ever losing his "short career" bonus vis-a-vis his annuity computation.

This approach constitutes an inducement for crossover, of varying intensity: the longer the employee has served; the greater the inducement. An FS employee with 20+ years of service will get up to 14% of salary more on his annuity for his post-crossover service than he would if pre-crossover service were counted against the 20 years of richer treatment in the new system (See Able). Employees with less pre-crossover service derive progressively less extra benefit from this treatment, since they would stand to get some 1.7% post-crossover credit regardless of the rules used (See Charles).